Energy Prepayment Review
Competition and Markets Authority
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Review of the Energy Market Investigation (Prepayment Charge Restriction) Order 2016 Provisional Decision

EDF Energy is one of the UK's largest energy companies with activities throughout the energy chain. Our interests include nuclear, coal and gas-fired electricity generation, renewables, storage, and energy supply to end users. We have around five million electricity and gas customer accounts in the UK, including residential and business users.

EDF Energy has fully supported the CMA undertaking a review of the current Prepayment Charge Restriction (PPM Cap) with a view to investigating whether any change in circumstance since its introduction would make the Energy Market Investigation (Prepayment Charge Restriction) Order 2016 (PPM Order) no longer appropriate and as such require it to be varied or revoked.

Variation to PPM Order

In responding to the CMA's earlier consultation on this matter we confirmed our view that there had been a relevant change in circumstance that would require a change to the PPM Order. Specifically, we considered that the introduction of Ofgem's Default Tariff Cap resulted in the existence of two caps with different methodologies that could have a detrimental impact on the incentives for customers to accept a smart meter. In addition, there were weaknesses in the current PPM Cap methodology resulting in actual costs significantly diverging from allowed costs, including smart costs.

Consequently, we called for the CMA to align the PPM Cap methodology with that of Ofgem's Default Tariff Cap methodology, with an adjustment to reflect the additional costs associated with serving legacy prepayment customers.

Given the above, we are supportive of the CMA's provisional conclusion that the PPM Cap is no longer effective in meeting its aims and that a variation to the Order is required. Furthermore, we broadly support the CMA's provisional decision on reform of the Order such that Ofgem's Default Tariff Cap methodology will be adopted with adjustments to reflect the specific costs in supplying prepayment customers. It is essential that this is implemented by October this year, as proposed, as the CMA has now recognised that the current methodology for the PPM cap does not allow suppliers to recover efficient costs.

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Treatment of Smart Metering Costs

However, we fundamentally oppose the CMA's proposed decision that smart metering 'non-pass through' costs should not be borne by prepayment customers under the PPM Cap. The CMA's rationale for this decision, specifically that customers with traditional prepayment meters should not contribute towards all the cost elements in the delivery of smart metering as they do not yet have smart meters themselves, runs counter to the basis on which the Government has established the smart metering programme. Government is clear that there is to be no upfront cost to customers accepting a smart meter, with the intention that the full costs of the programme will be socialised across all consumers - whether or not they have accepted a smart meter[1].

We have consistently raised concerns about the under recovery of smart metering costs within the CMA's PPM Cap given the methodology used, including because that methodology does not recognise smart metering as a distinct cost component.

We note that during design development of both the extended Safeguard Tariff and the Default Tariff Cap, Ofgem considered the potential to adopt the PPM Cap methodology. However, in light of stakeholder feedback on the weaknesses of such an approach, Ofgem opted to include smart metering costs, based on suppliers' actual cost information, in the 'operating costs' baseline, and then to use a separate smart metering increment to vary the allowance to reflect the net change in smart costs year on year. To be clear, in setting the level of the Default Tariff Cap, Ofgem adopted a methodology whereby smart metering costs (both pass through and non-pass through) are recovered across the total national residential customer base.

Consequently, the CMA's provisional decision is inconsistent with the approach implemented by Ofgem and would result in suppliers being left with unacceptable stranded costs relating to the costs to the smart metering rollout (including the cost of the metering assets, installation, In Home Display and smart-related system changes, as well as supplier-led customer engagement activity). We would urge the CMA to reconsider its position in respect of non-pass through costs and recognise that suppliers should recover their full efficient smart metering costs from their whole portfolio of residential customers, as envisaged by both Government and Ofgem.

Capacity Market Costs

As outlined above it is essential that the CMA meets its aim of adopting its final decision in time for it to be applied in calculating the level of the PPM Cap for the next charge restriction period commencing in October 2019 in order that suppliers can recover their efficient costs. If this timescale is not achieved, then the CMA will need to address the fact that the PPM Cap will not include relevant Capacity Market (CM) costs. This is because the latest OBR forecasts, as used in the PPM Cap model, do not include CM costs, given the standstill period for the CM scheme. As a consequence, under the current PPM

[1] Under Electricity Standard Licence Condition 41.8 Suppliers are required to ensure that the costs of smart metering are borne by the licensee's Domestic Customers generally as an increment of charges for electricity supplied.

Cap methodology, CM costs would not be included when indexing policy costs for the cap period starting in October 2019.

Under the Default Tariff Cap, Ofgem is proposing to include a full CM allowance in the cap level for the period commencing in October 2019, as it did for the current period. This is due to the fact that the government has expressed confidence that the European Commission will grant state aid clearance of the CM by October 2019. The Government has made clear that suppliers will be expected to pay the CM charge once the scheme is reinstated, including for the period when payments to capacity agreement holders have been suspended, and has put in place mechanisms to enable the money to be collected from suppliers. Ofgem's proposal on the Default Tariff Cap is based on the assumption that there will not be a State Aid decision prior to it setting the cap level.

Consequently, we believe the CMA needs to duly consider this risk and ensure that CM costs will be recovered under both caps. This may for instance include a Direction to Ofgem to use an alternative data source in respect of CM costs when calculating the policy cost index value, if the implementation of changes proposed in this provisional decision is delayed.

Should you wish to discuss any of the issues raised in our response or have any queries, please contact Steven Eyre on 0208 186 1356, or myself on 07875 112625.

Yours sincerely,

[redacted]

Rebecca Beresford
Head of Customers Policy and Regulation